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C O N F I D E N T I A L SECTION 01 OF 03 PRAGUE 000115

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TAGS: TRGY ENRG BTIO PREL TNGD BEXP EZ
SUBJECT: FEELING THE BURN: RENEWABLES TARGETS AND SOLAR INCENTIVES

Classified By: CDA Mary Thompson-Jones for reasons 1.4 (b) and (d)

¶1. (C) Summary: The Czech government's response to EU-set targets for increased use of renewable energy sources (RES) to meet electricity needs has been lackluster and expensive. Renewables' share in electricity consumption increased last year mainly due to a recession-driven decrease in total electricity consumption, and RES still only account for a small portion of total electricity consumed. A sudden reduction in the cost of solar equipment has led to an exponential growth in solar energy generation, rendering the current subsidy system unsustainable. Solar plants continue to increase in number, despite being the least financially efficient energy source in the Czech Republic. Both national and local authorities remain suspicious of renewables. The Czech Republic is unlikely to meet its EU-mandated RES targets without a change in public attitude and significant reworking of its RES subsidy policy. End Summary.

Mostly Coal, but Renewables are on the Rise

¶2. (SBU) Coal accounts for roughly 50 percent of the total Czech energy supply and around 60 percent of electricity generation. The remaining portion of electricity comes primarily from nuclear power (about 32 percent) with RES composing just over 5 percent (as of the end of 2008). Within the realm of RES, hydroelectric power plants dominate production (54 percent of RES, 2.4 percent of total electricity production), followed by biomass (1.4 percent of total electricity), then biogas and wind power (about 0.3 percent of total electricity each), and finally photovoltaic or solar energy, composing a mere 0.02 percent of electricity generation in 2008. Past proposals to change the Czech energy and electricity composition have been aimed primarily at energy modernization and security, namely increased reliance on nuclear energy, reduced reliance on coal, and increased access to non-Russian natural gas sources.

¶3. (SBU) Increased investment in RES in the Czech Republic (CR) has come largely in response to EU directives intended to lower greenhouse gas emissions and promote RES. The CR faces EU-set mandatory targets of 8 percent reliance on RES for gross electricity consumption by 2010 and 13 percent by ¶2020. While an official Czech Industry and Trade Ministry report called the 2010 target "overly ambitious," some officials still believe it to be feasible. The share of renewable energy in electricity consumption has risen steadily (albeit modestly) over the past five years from 4.0 percent in 2004 to 5.2 percent in 2008.

Incentives for RES Producers

¶4. (SBU) In 2005, the CR instituted a series of incentives (which are still in place) to encourage investment in RES

technology and production of energy from RES. In addition to the guarantee that the relevant regional distribution company purchase energy produced from RES, the law stipulates that ancillary costs of RES energy production be passed on to the consumer via higher energy prices, rather than reduce RES company profit margins. Even more significant, producers can choose between receiving green bonuses (an amount paid to the supplier above the market price of electricity) or feed-in tariffs (fixed minimum purchase prices for energy supplied). The central Energy Regulatory Office sets the latter, and the law guarantees that the fixed minimum price not drop more than five percent year-on-year. According to Industry and Trade Ministry Renewable Energy Department Head Ondrej Tomsej, the feed-in tariffs are significantly more popular among investors. Since 2005, producers have also been eligible for additional, specific subsidies offered through different programs by the Ministry of Industry and Trade, the Environment Ministry, and EU structural funds.

¶5. (SBU) Incentives succeeded in stimulating construction and expansion of facilities harnessing biomass, photovoltaics, biogas, and wind capacity. The share of gross electricity consumption derived from RES increased from 4.74 percent in 2007 to 5.18 percent in 2008. Unofficial Industry and Trade Ministry estimates put RES share of electricity at 6.8 percent in 2009, though according to Tomsej, most of the increase is attributable to a drop in energy consumption caused by the economic recession. In 2009 the Czech economy contracted 4.2 percent and energy consumption fell about 4.8 percent. Among the RES, photovoltaic electricity production showed the most dramatic rise (514 percent), but still only accounted for about 0.02 percent of gross electricity

consumption in 2008 and an estimated 0.13 percent in 2009.

¶6. (C) According to energy expert Bretislav Dancak, the Czech energy mix is largely unaffected by these developments, and is unlikely to change significantly in the future. Dancak dismissed RES incentives as a government effort to "look busy" for the EU; furthermore the renewables industry will not flourish in the CR because CEZ, the semi-state owned electricity company with a notoriously heavy hand in Czech politics, has no vested interest in its success. Michal Janecek, owner of one of the largest solar plants in the Czech Republic and Chairman of the Czech Wind Energy Association, echoed Dancak's skepticism of the government's commitment. He added that the CSSD-led government passed legislation in 2005 intended to support growth in the renewables sector. When the ODS government took over in 2006, however, momentum for renewable energy growth decreased considerably and the support on the books did not translate into support in practice, but rather hostility towards renewables. The Fisher-led, interim government of the past ten months, according to Janecek, provided a neutral space for the solar industry to "boom" unhindered.

Why Solar?

¶7. (SBU) The number of solar power plants grew more than tenfold in the CR over the last two years. As of November 1, 2009, there are 3,136 solar power plants in the CR with a total output, according to the Ecological Alternatives League, of over 133 megawatts. Experts attribute the precipitous increase in solar plant construction and investment to the confluence of high, fixed solar power rates and a large drop in the cost of photovoltaic panels. A change in Spain's solar energy policy in 2008, for instance, led to the availability of solar panels at "dumping" prices, according to Janecek. Daniel Kunz, CEO of leading renewable energy company Energy 21, told press that the payback period for solar power plants has shortened to 8-10 years, now that technology costs have fallen 40 percent since 2007, and there has been no commensurate purchase price adjustment. The

result has been a rush of investors from the wind sector to the solar sector, as well as hundreds of new investors from other industries.

¶8. (SBU) Other major RES each face unique obstacles to growth. The CR has already harnessed the majority of its hydroelectric potential, leaving little room for growth regardless of the incentives. Electricity produced from biomass saw a 20 percent increase in 2008. However, most energy produced by biomass is harnessed for heat rather than electricity. In addition, while policy-makers believe that biomass holds the greatest potential for expansion in the CR, development of biomass capacity is still not economically attractive even with the current incentives.

¶9. (C) Wind energy production has increased as a result of the government incentives, however experts believe its continued growth potential to be limited. Regional governments also often object to the construction of wind turbines in their districts, citing their visual and noise implications. In addition, Industry and Trade Ministry officers have claimed that there is "insufficient" wind. Critics of wind energy also explain that managing the spikes and dips of energy generated by wind power is both difficult and expensive for grid operation.

¶10. (C) Wind farm operator KV Venti's CEO, David Jozevsky, calls these claims "nonsense." Mr. Jozevsky, whose company operates three wind facilities in the Czech Republic and a handful abroad, told us that the central government is attempting to avoid confrontation with regional governments on this topic, and do not themselves want wind turbines erected near their out-of-Prague, pastoral summerhomes. Janecek told us that local government "obstructionism" led to a five to six year period between conception and operation of wind plants (as opposed to the twelve to eighteen month period for solar plants). Janecek partly attributes the wind-to-solar brain drain of the last two years to this undue bureaucracy.

Sustainable Energy Policy "Unsustainable"

¶11. (U) On November 30, Roman Polak of the Energy Regulatory Office (ERU) told the press that photovoltaics is one of the least effective electricity sources, but receives some 40 percent of the support designated for all RES. However, with

the ostensible money-back-guarantee on solar plant investment, facilities continue to crop up around the CR, with little effect on overall energy supply. Critics of solar power note that the price paid for solar energy is 14 times the price of energy from coal and nuclear and 4.5 times the cost of wind power. Industry and Trade Minister Vladimir Tolovsky announced that the enormous rise in subsidized energy production, particularly solar energy, could drive up the residential price of electricity 19 percent by 2012. He warned that industrial energy cost could rise 50 percent and repel potential foreign investment.

¶12. (C) Politicians, analysts, and journalists are demanding renewables policy reform, calling the current system financially unsustainable. The leading national economic newspaper's energy reporter told us that even the main Czech photovoltaic trade association accepts that reform is necessary, though the details will require further discussion. On February 8, the Czech Cabinet released a list of short-term priorities, including passage of reform legislation during the first half of 2010 to reduce solar subsidies. Mr. Tomsej also told us that the Industry and Trade Ministry submitted a legislative proposal to the government to allow the fixed minimum price to drop by more than 5 percent, and expects that the Chamber of Deputies will give this proposal a second reading this spring.

¶13. (C) Technical concerns exist as well. The Czech electricity grid operator (CEPS) warned in early February that the additional grid connections required to service the thousands of low-yield plants have exceeded the number consistent with the safe and reliable operation of the power grid. On February 16, Czech electricity distribution companies stopped accepting new applications to join the grid. Janecek told us that government warnings of blackouts due to an overloaded grid are nothing more than fear-mongering and an attempt to avoid the appearance of welching on its commitment to subsidize clean energy. According to Janecek, the government announced last year that the grid could accommodate 2000 megawatts of new connections; now, only 600 megawatts later, the grid is allegedly full.

Paying More for the Same Pie

¶14. (C) Comment: Czech efforts to increase reliance on RES for electricity consumption (whether sincere or not) have produced only modest changes to the national energy mix, but could cause dramatic increases to energy cost. While investors in solar would likely perceive a sudden drop in fixed purchase prices as a betrayal, the government, the consumer, and the investment climate cannot afford the alternative: a dramatic rise in energy prices for everyone. Alleged grid problems will help to justify discontinuation of new licenses, though, for legal reasons, the current incentives will probably have to be grandfathered for existing producers. However, if the Czech Republic is serious about increasing its reliance on renewable energy, it will need to develop a new structure that encourages investment in more promising technologies such as biomass. End Comment.
Thompson-Jones